

K-Bro Linen Income Fund

Interim Consolidated Financial Statements
September 30, 2009

K-Bro Linen Income Fund

Interim Consolidated Balance Sheets

	September 30, 2009 \$ (Unaudited)	December 31, 2008 \$ Restated (see note 3)
Assets		
Current assets		
Accounts receivable	9,046,609	8,669,939
Linen in service	7,243,975	7,755,839
Prepaid expenses and deposits	1,095,774	623,953
Future income taxes	558,405	426,032
	<u>17,944,763</u>	<u>17,475,763</u>
Restricted escrow funds (note 4)	-	540,500
Property, plant and equipment	34,944,136	36,024,039
Intangible assets	14,455,363	16,073,218
Goodwill	16,220,250	15,679,750
	<u>83,564,512</u>	<u>85,793,270</u>
Liabilities and Unitholders' Equity		
Current liabilities		
Accounts payable and accrued liabilities	9,561,076	12,884,895
Distribution payable to unitholders	642,146	642,146
	<u>10,203,222</u>	<u>13,527,041</u>
Long-term debt	5,106,967	4,061,285
Unamortized lease inducements	477,970	520,144
Future income taxes	4,091,376	3,919,231
	<u>19,879,535</u>	<u>22,027,701</u>
Contingencies and commitments (note 6)		
Unitholders' Equity		
Exchangeable shares (note 7b)	724,110	724,110
Fund units (note 7b)	70,675,516	70,675,516
Fund units held in trust by LTIP	(834,137)	(457,079)
Contributed surplus (note 7c)	509,215	340,728
Deficit	(7,330,146)	(7,405,966)
Accumulated other comprehensive loss (note 7d)	(59,581)	(111,740)
	<u>63,684,977</u>	<u>63,765,569</u>
	<u>83,564,512</u>	<u>85,793,270</u>

The accompanying notes are an integral part of these consolidated financial statements.

Approved on behalf of the Fund

(Signed) "Ross Smith"

Trustee

(Signed) "Matthew Hills"

Trustee

K-Bro Linen Income Fund

Interim Consolidated Statements of Earnings and Deficit

(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2009 \$	2008 \$ Restated (see note 3)	2009 \$	2008 \$ Restated (see note 3)
Revenue	22,659,028	22,063,179	65,898,373	63,566,524
Expenses				
Wages and benefits	10,291,687	10,117,790	29,713,610	30,210,931
Linen	2,568,886	2,592,690	7,686,722	7,653,288
Utilities	1,528,325	1,619,427	4,655,949	5,048,430
Delivery	852,459	911,345	2,430,003	2,743,886
Repairs and maintenance	818,083	773,010	2,356,747	2,137,215
Materials and supplies	786,604	679,856	2,368,815	1,948,268
Occupancy costs	759,381	924,712	2,208,377	2,458,573
Corporate	915,853	847,509	2,737,601	2,295,672
	18,521,278	18,466,339	54,157,824	54,496,263
Earnings before the undernoted	4,137,750	3,596,840	11,740,549	9,070,261
Other expenses				
Amortization of property, plant and equipment	(1,345,539)	(1,363,952)	(4,029,356)	(3,641,631)
Amortization of intangible assets	(539,285)	(539,285)	(1,617,855)	(1,610,693)
Financial charges	(60,383)	(147,660)	(214,947)	(544,868)
(Loss) gain on disposal of property, plant and equipment	(362)	550	(3,679)	(457,343)
Write-off of new plant start-up costs (note 3)	-	-	-	(132,631)
	(1,945,569)	(2,050,347)	(5,865,837)	(6,387,166)
Earnings before income taxes	2,192,181	1,546,493	5,874,712	2,683,095
Income tax (expense) recovery	(96,617)	63,784	(19,579)	654,389
Net earnings for the period	2,095,564	1,610,277	5,855,133	3,337,484
Deficit – beginning of period	(7,499,272)	(6,547,755)	(7,405,966)	(4,573,837)
Distributions to unitholders (note 8)	(1,926,438)	(1,926,437)	(5,779,313)	(5,627,562)
Deficit – end of period	(7,330,146)	(6,863,915)	(7,330,146)	(6,863,915)
	\$	\$	\$	\$
Net earnings per unit				
Basic	0.30	0.23	0.84	0.48
Diluted	0.30	0.23	0.83	0.48
	#	#	#	#
Weighted average number of units outstanding				
Basic	6,929,824	6,969,420	6,950,274	6,951,816
Diluted	6,994,005	6,996,177	7,014,454	6,978,573

The accompanying notes are an integral part of these consolidated financial statements.

K-Bro Linen Income Fund

Interim Consolidated Statements of Comprehensive Income

(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2009 \$	2008 \$ Restated (see note 3)	2009 \$	2008 \$ Restated (see note 3)
Net earnings for the period	2,095,564	1,610,277	5,855,133	3,337,484
Other comprehensive income (loss) (Loss) gain on derivative instruments designated as cash flow hedges, net of future income taxes of \$2,113 (nine months ended September 30, 2009 – (\$20,193); three months ended September 30, 2008 – \$9,009; nine months ended September 30, 2008 – \$13,179)	<u>(5,527)</u>	<u>(20,356)</u>	<u>52,159</u>	<u>(29,716)</u>
Other comprehensive (loss) income for the period	<u>(5,527)</u>	<u>(20,356)</u>	<u>52,159</u>	<u>(29,716)</u>
Comprehensive income for the period	<u>2,090,037</u>	<u>1,589,921</u>	<u>5,907,292</u>	<u>3,307,768</u>

The accompanying notes are an integral part of these consolidated financial statements.

K-Bro Linen Income Fund

Interim Consolidated Statements of Cash Flows (Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2009 \$	2008 \$ Restated (see note 3)	2009 \$	2008 \$ Restated (see note 3)
Cash provided by (used in)				
Operating activities				
Net earnings for the period	2,095,564	1,610,277	5,855,133	3,337,484
Items not affecting cash				
Amortization of property, plant and equipment	1,345,539	1,363,952	4,029,356	3,641,631
Amortization of intangible assets	539,285	539,285	1,617,855	1,610,693
Amortization of lease inducements	(14,058)	(14,058)	(42,174)	(28,116)
Loss (gain) on disposal of property, plant and equipment	362	(550)	3,679	457,343
Future income taxes	96,617	(63,784)	19,579	(654,389)
	4,063,309	3,435,122	11,483,428	8,364,646
Net change in non-cash working capital items (note 9)	1,504,950	2,134,575	(3,172,200)	1,363,477
Cash provided by operating activities	5,568,259	5,569,697	8,311,228	9,728,123
Financing activities				
(Decrease) increase in long-term debt – revolving line of credit	(1,627,584)	(2,790,864)	1,045,682	(10,408,063)
Distributions paid to unitholders	(1,926,438)	(1,926,437)	(5,779,313)	(5,489,259)
Fund units issued – net of offering costs	-	-	-	18,092,544
Cash provided by (used in) financing activities	(3,554,022)	(4,717,301)	(4,733,631)	2,195,222
Investing activities				
Purchase of property, plant and equipment	(2,014,237)	(854,995)	(3,584,097)	(8,239,361)
Proceeds from disposal of property, plant and equipment	-	2,599	6,500	158,760
Business acquisition	-	-	-	(3,302,244)
Escrow funds	-	-	-	(540,500)
Cash used in investing activities	(2,014,237)	(852,396)	(3,577,597)	(11,923,345)
Change in cash	-	-	-	-
Cash – beginning of period	-	-	-	-
Cash – end of period	-	-	-	-
Supplementary cash flow information				
Interest paid	85,622	112,654	244,256	454,029
Non-cash financing and investing activities				
Equipment purchases included in accounts payable and accrued liabilities	459,298	1,365,942	459,298	1,365,942
Distribution included in distribution payable	-	-	-	138,303

The accompanying notes are an integral part of these consolidated financial statements.

K-Bro Linen Income Fund

Notes to Interim Consolidated Financial Statements

(Unaudited)

September 30, 2009

1 Business description

K-Bro Linen Income Fund (the “Fund”) is a limited purpose trust established under the laws of Alberta pursuant to the Amended and Restated Fund Declaration of Trust dated February 3, 2005. The Fund was created for the purpose of acquiring, directly or indirectly, all of the issued and outstanding securities of K-Bro Linen Systems Inc. K-Bro Linen Systems Inc. provides a range of services to healthcare institutions, hotels and other commercial accounts. These services include the processing, management and distribution of linen.

2 Basis of presentation

These accompanying unaudited interim consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles (“GAAP”) for interim financial statements. The accounting principles and methods of computation adopted in these financial statements are the same as those of the audited consolidated financial statements for the fiscal year ended December 31, 2008 except as described in Note 3. However, these interim consolidated financial statements do not include all information and disclosures required under GAAP for annual financial statements. Accordingly, these unaudited consolidated interim financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto for the year ended December 31, 2008.

3 Changes in accounting policies

Goodwill and intangible assets

In February 2008, the CICA issued a new accounting standard – Section 3064 “Goodwill and intangible assets” replacing accounting standards Section 3062 “Goodwill and other intangible assets” and Section 3450 “Research and development costs.” Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. The new Section is applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. Accordingly, the Fund adopted the new standard for its fiscal year beginning January 1, 2009. The provisions of Section 3064 were adopted retrospectively, with restatement of prior periods.

As a result of this adoption, the Fund has retroactively expensed certain expenditures related to the pre-operating period of the new Calgary plant, rather than recording them as assets in “Deferred charges.” The adoption of Section 3064 resulted in an increase to opening deficit of \$nil at January 1, 2008 and \$96,217 at January 1, 2009. For the three months ended September 30, 2008, the adoption of this standard resulted in no change to the statement of earnings or the earnings per unit. For the nine months ended September 30, 2008, the adoption of this standard resulted in an increase of \$132,631 in the “Write-off of new plant start-up costs” expense and an increase in the “Future income tax recovery” of \$36,414, and reduced both basic and diluted earnings per unit by \$0.01.

K-Bro Linen Income Fund

Notes to Interim Consolidated Financial Statements

(Unaudited)

September 30, 2009

4 Business acquisition

On January 31, 2008, the Fund completed the acquisition of the laundry business, linen, property and equipment of Buanderie HMR Inc. located in Quebec City, Quebec. The business acquisition was accounted for using the purchase method, whereby the purchase consideration was allocated to the fair values of the net assets acquired at January 31, 2008. The allocation was based on management's best estimate of the fair value of net assets acquired.

Of the cash consideration payable to the vendor, \$540,000 was deposited into escrow with an escrow agent. The funds held in escrow were to be released to the vendor upon the determination that specified earnings before interest, income taxes and amortization were met in the twelve-month period subsequent to the acquisition and goodwill correspondingly increased by the amount released. As at March 30, 2009 it was determined that the \$540,000 was eligible for release and goodwill has been correspondingly increased.

5 Future income taxes

On June 12, 2007, Bill C-52 Budget Implementation Act 2007, which contains legislation to tax publicly traded trusts in Canada, was substantively enacted by the Canadian Federal Government. As a result, a new 31.5 per cent tax will be applied to distributions from Canadian public income trusts. The new tax is not expected to apply to the Fund until 2011 as a transition period applies to publicly traded trusts that existed prior to November 1, 2006. There was no additional future income tax expense or recovery that needed to be recorded by the Fund as a result of this legislation as future income taxes are already recorded by the Fund's wholly-owned subsidiary K-Bro Linen Systems Inc.

6 Contingencies and commitments

a) Contingencies

Letters of credit

The Fund has an outstanding letter of credit issued as part of normal business operations in the amount of \$250,000 (2008 – \$250,000) expiring January 24, 2010. A \$185,000 letter of credit outstanding at December 31, 2008 was cancelled in March 2009.

K-Bro Linen Income Fund

Notes to Interim Consolidated Financial Statements

(Unaudited)

September 30, 2009

b) Commitments

Operating leases and utility commitments

Minimum lease payments for operating leases on buildings and equipment and estimated natural gas and electricity commitments for the next five calendar years are as follows:

	\$
Remainder of 2009	1,351,824
2010	3,311,916
2011	2,084,295
2012	2,002,862
2013	1,782,979
Subsequent	3,973,831

Linen purchase commitments

At September 30, 2009, the Fund was committed to linen expenditure obligations in the amount of \$1,310,203 (December 31, 2008 – \$2,196,023).

K-Bro Linen Income Fund

Notes to Interim Consolidated Financial Statements

(Unaudited)

September 30, 2009

7 Unitholders' equity

a) Authorized

The declaration of trust provides that an unlimited number of units and an unlimited number of Special Trust Units may be issued.

b) Issued and outstanding

Fund Units	#	\$
Balance at December 31, 2007	<u>5,423,862</u>	<u>52,210,472</u>
Issued on February 27, 2008 at \$12.85 per Unit	1,362,000	17,501,700
Offering costs – net of future tax recovery of \$341,000		(842,959)
Issued on March 28, 2008 at \$12.85 per Unit	146,700	1,885,095
Offering costs – net of future tax recovery of \$31,500		(78,792)
	<u>1,508,700</u>	<u>18,465,044</u>
Balance at September 30, 2009 and December 31, 2008	6,932,562	<u>70,675,516</u>
Exchangeable shares	#	\$
Balance at September 30, 2009 and December 31, 2008	<u>72,411</u>	<u>724,110</u>
Total Fund Units and Exchangeable shares issued	<u>7,004,973</u>	

The exchangeable shares were issued by the Fund's subsidiary to certain members of management and are exchangeable on a one-to-one basis for Fund Units. The risks and privileges of these shares are the same as for Fund Units. The exchangeable shares of the Fund's subsidiary are synonymous with the Special Trust Units of the Fund.

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c) Contributed surplus

	Nine months ended September 30, 2009 \$	Year ended December 31, 2008 \$ (Audited)
Balance, beginning of period	340,728	413,671
Net stock based compensation recorded	587,569	319,628
Issuance of vested Units to participants	<u>(419,082)</u>	<u>(392,571)</u>
Balance, end of period	<u>509,215</u>	<u>340,728</u>

d) Accumulated other comprehensive loss

	Nine months ended September 30, 2009 \$	Year ended December 31, 2008 \$ (Audited)
Balance, beginning of period	(111,740)	1,899
Other comprehensive income (loss) during the period	<u>52,159</u>	<u>(113,639)</u>
Balance, end of period	<u>(59,581)</u>	<u>(111,740)</u>

8 Distributions to unitholders

The Fund's policy is to make distributions to unitholders of its available cash to the maximum extent possible consistent with good business practice considering requirements for capital expenditures, working capital, growth capital and other reserves considered advisable by the Trustees of the Fund. All such distributions are discretionary. Distributions are declared payable each month to the Fund unitholders and exchangeable shareholders on the last business day of each month and are paid by the 15th day of the following month.

Distributions declared during the nine months ended September 30, 2009 were at the rate of \$0.09167 per unit per month (\$1.10 per unit annualized) for a total declared distribution of \$5,779,313 (nine months ended September 30, 2008 – \$5,627,562).

K-Bro Linen Income Fund

Notes to Interim Consolidated Financial Statements

(Unaudited)

September 30, 2009

9 Net change in non-cash working capital items

	Three months ended September 30,	
	2009	2008
	\$	\$
		Restated (see note 3)
Cash provided (used) by changes in		
Accounts receivable	393,408	(184,837)
Linen in service	85,175	493,572
Prepaid expenses and deposits	(314,585)	202,441
Accounts payable and accrued liabilities	1,340,952	1,623,399
	<u>1,504,950</u>	<u>2,134,575</u>

	Nine months ended September 30,	
	2009	2008
	\$	\$
		Restated (see note 3)
Cash provided (used) by changes in		
Accounts receivable	(376,670)	(811,748)
Linen in service	511,864	1,067,386
Prepaid expenses and deposits	(471,821)	169,998
Accounts payable and accrued liabilities	(2,835,573)	937,841
	<u>(3,172,200)</u>	<u>1,363,477</u>

10 Segmented information

The Fund provides laundry and linen services to the healthcare and hospitality sectors through six operating segments in Vancouver, Victoria, Calgary, Edmonton, Toronto and Quebec City. The services offered and the economic characteristics associated with these segments are similar, therefore these segments have been aggregated into one reportable segment which operates exclusively in Canada. The results of the Quebec City operation acquired (see note 4) are reported commencing February 1, 2008.

K-Bro Linen Income Fund

Notes to Interim Consolidated Financial Statements

(Unaudited)

September 30, 2009

Total revenue derived from the healthcare and hospitality sectors are as follows:

	Three months ended September 30, 2009		September 30, 2008	
Healthcare	16,524,395		16,225,533	
Hospitality	6,134,633		5,837,646	
	<hr/>		<hr/>	
Total	22,659,028		22,063,179	
	<hr/>		<hr/>	
	Nine months ended September 30, 2009		September 30, 2008	
Healthcare	50,185,055		47,915,798	
Hospitality	15,713,318		15,650,726	
	<hr/>		<hr/>	
Total	65,898,373		63,566,524	
	<hr/>		<hr/>	

In Edmonton, the Fund is the significant supplier of laundry and linen services to the entity which manages all major healthcare facilities in the region. This contract expires on December 31, 2010. In Calgary, the major customer is contractually committed to February 28, 2018 and in Vancouver the major customer is contractually committed to January 15, 2013.

For the nine months ended September 30, 2009, the Fund has recorded revenue of \$39.1 million (nine months ended September 30, 2008 – \$36.5 million) from these three major customers, representing 59% (2008 – 57%) of total revenue.

11 Related party transaction

The Fund has incurred expenses in the normal course of business for advisory consulting services provided by a Trustee primarily relating to acquisitions. The amounts charged are recorded at their exchange amounts and are subject to normal trade terms. For the three months ended September 30, 2009, the Fund incurred such fees totalling \$34,500 (three months ended September 30, 2008 – \$11,500). For the nine months ended September 30, 2009, the Fund incurred such fees totalling \$103,500 (nine months ended September 30, 2008 – \$39,500).

12 Comparative figures

Certain of the comparative figures have been reclassified to conform to the presentation for the current period.